KPMG

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Independent Auditors' Report

Division of Retirement and Benefits
Members of the Alaska Public Employees' Retirement Board and
State of Alaska Public Employees' Retirement System:

We have audited the accompanying combining statements of plan net assets of the State of Alaska Public Employees' Retirement System (Plan), a Component Unit of the State of Alaska, as of June 30, 2001 and 2000, and the related combining statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combining financial statements referred to above present fairly, in all material respects, the plan net assets of the State of Alaska Public Employees' Retirement System, a Component Unit of the State of Alaska, as of June 30, 2001 and 2000, and the changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The required supplementary information on pages 32 to 38 and additional information on pages 39 and 40 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information is the responsibility of the Plan's management, has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The investment, actuarial and statistical data on pages 41 through 85 are presented for the purpose of additional analysis and are not a required part of the basic financial statements of the State of Alaska Public Employees' Retirement System (Plan), a Component Unit of the State of Alaska. Such additional information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

September 25, 2001

KPMG LLP

STATE OF ALASKA
PUBLIC EMPLOYEES' RETIREMENT SYSTEM
(A Component Unit of the State of Alaska)

Combining Statements of Plan Net Assets

June 30, 2001 and 2000
(000's omitted)

	2001			2000		
	Pension	Postemployment Healthcare	Total	Pension	Postemployment Healthcare	Total
Assets:						
Cash and cash equivalents (notes 3 and 4):						
Short-term fixed income pool	$ 377	153	530	387	157	544
Receivables:						
Contributions	6,605	2,684	9,289	5,571	2,264	7,835
Retirement Incentive Program employer contributions (note 7)	3,749	1,524	5,273	9,975	4,054	14,029
Due from State of Alaska General Fund	585	237	822	1,993	810	2,803
Other accounts receivable	1	1	2	1	-	1
Total receivables	10,940	4,446	15,386	17,540	7,128	24,668
Investments, at fair value (notes 3 and 4):						
Domestic equity pool	2,417,050	918,940	3,335,990	2,715,529	1,038,516	3,754,045
Retirement fixed income pool	1,471,224	597,892	2,069,116	1,548,724	629,388	2,178,112
International equity pool	942,673	383,094	1,325,767	1,127,422	458,175	1,585,597
Real estate pool	418,479	170,066	588,545	332,616	135,173	467,789
International fixed income pool	273,627	111,200	384,827	286,226	116,319	402,545
Private equity pool (note 8)	146,805	59,660	206,465	117,155	47,611	164,766
Emerging markets equity pool	51,591	20,966	72,557	69,429	28,215	97,644
External domestic fixed income pool	69,249	28,143	97,392	61,811	25,120	86,931
Total investments	5,790,698	2,289,961	8,080,659	6,258,912	2,478,517	8,737,429
Loans and mortgages, at fair value, net of allowance for loan losses of $202 in 2001, and 2000	248	101	349	402	163	565
Total assets	5,802,263	2,294,661	8,096,924	6,277,241	2,485,965	8,763,206
Liabilities:						
Accrued expenses	6,068	2,466	8,534	4,696	1,908	6,604
Alaska Department of Commerce escrow liability	6	2	8	16	6	22
Total liabilities	6,074	2,468	8,542	4,712	1,914	6,626
Commitments and Contingencies (note 8)						
Net assets held in trust for pension and postemployment healthcare benefits	**$5,796,189**	**2,292,193**	**8,088,382**	**6,272,529**	**2,484,051**	**8,756,580**

(Schedules of funding progress are presented on pages 32 and 33)

See accompanying notes to combining financial statements.

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Combining Statements of Changes in Plan Net Assets

Years ended June 30, 2001 and 2000
(000's omitted)

	2001			2000		
	Pension	Postemployment Healthcare	Total	Pension	Postemployment Healthcare	Total
Additions:						
Contributions:						
Employers	$ 68,604	27,880	96,484	66,637	27,079	93,716
Plan members	67,537	27,446	94,983	65,387	26,573	91,960
Retirement Incentive Program - Employers (note 7)	-	-	-	9,869	4,011	13,880
Retirement Incentive Program - Plan members (note 7)	-	-	-	576	234	810
Total contributions	136,141	55,326	191,467	142,469	57,897	200,366
Investment income:						
Net appreciation (depreciation) in fair value of investments (note 3)	(558,855)	(227,114)	(785,969)	365,752	148,638	514,390
Interest	125,703	51,085	176,788	134,682	54,734	189,416
Dividends	107,221	43,574	150,795	75,215	30,567	105,782
Net recognized mortgage loan recovery	-	-	-	234	95	329
	(325,931)	(132,455)	(458,386)	575,883	234,034	809,917
Less investment expense	14,123	5,740	19,863	13,923	5,658	19,581
Net investment income (loss)	(340,054)	(138,195)	(478,249)	561,960	228,376	790,336
Other	5	2	7	-	-	-
Total additions	(203,908)	(82,867)	(286,775)	704,429	286,273	990,702
Deductions:						
Benefits	259,771	103,846	363,617	239,441	83,794	323,235
Refunds of contributions	9,339	3,795	13,134	8,531	3,467	11,998
Administrative expenses	3,322	1,350	4,672	3,020	1,227	4,247
Total deductions	272,432	108,991	381,423	250,992	88,488	339,480
Net increase (decrease)	(476,340)	(191,858)	(668,198)	453,437	197,785	651,222
Net assets held in trust for pension and postemployment healthcare benefits:						
Balance, beginning of year	6,272,529	2,484,051	8,756,580	5,819,092	2,286,266	8,105,358
Balance, end of year	**$5,796,189**	**2,292,193**	**8,088,382**	**6,272,529**	**2,484,051**	**8,756,580**

See accompanying notes to combining financial statements.

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Notes to Combining Financial Statements

June 30, 2001 and 2000
(000's omitted)

(1) DESCRIPTION

The following brief description of the State of Alaska Public Employees' Retirement System (Plan), a Component Unit of the State of Alaska, is provided for general information purposes only. Participants should refer to the Plan agreement for more complete information.

(a) General

The Plan is a defined benefit, agent, multiple employer public employee retirement system established and administered by the State of Alaska (State) to provide pension and postemployment healthcare benefits for eligible State and local government employees. Benefit and contribution provisions are established by State law and may be amended only by the State Legislature. The Plan is considered a component unit of the State financial reporting entity and is included in the State's financial reports as a pension trust fund. The State employees who administer the Plan participate in the Plan.

At June 30, 2001 and 2000, the number of participating local government employers and public organizations including the State was:

	2001	2000
State of Alaska	1	1
Municipalities	75	73
School districts	47	50
Other	27	27
	150	**151**

Inclusion in the Plan is a condition of employment for eligible State employees, except, as otherwise provided, for judges, elected officers and certain employees of the Alaska Marine Highway System. Any local government in the State may elect to have its permanent general and police and fire department employees covered by the Plan. At June 30, 1999 and 1998, the dates of the most recent actuarial valuations, Plan membership consisted of:

	1999	1998
Retirees and beneficiaries currently receiving benefits	14,185	13,101
Terminated Plan members entitled to future benefits	5,395	5,143
	19,580	18,244
Current Plan members:		
General	29,590	29,293
Police and fire	2,624	2,617
	32,214	31,910
	51,794	**50,154**
Current Plan members:		
Vested:		
General	17,254	17,335
Police and fire	1,781	1,799
Nonvested:		
General	12,336	11,958
Police and fire	843	818
	32,214	**31,910**

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The most recent actuarial valuation as of June 30, 2000, did not include participant census information subsequent to June 30, 1999.

(b) Pension Benefits

Employees hired prior to July 1, 1986, with five or more paid-up years of credited service are entitled to monthly pension benefits beginning at normal retirement age, fifty-five, or early retirement age, fifty. For employees first hired after June 30, 1986, the normal and early retirement ages are sixty and fifty-five, respectively. Employees with thirty or more years of credited service (twenty years for peace officers and firefighters) may retire at any age and receive a normal benefit.

The normal monthly pension benefit is based on years of service and average monthly compensation. For employees hired prior to July 1, 1996, the average monthly compensation is based upon the employees' three highest, consecutive years salaries. For employees hired after June 30, 1996, average monthly compensation is based upon the employees' five highest, consecutive years salaries.

The benefit related to all years of service prior to July 1, 1986, and for years of service through a total of ten years for general employees is equal to 2% of the employee's average monthly compensation for each year of service. The benefit for each year over ten years of service subsequent to June 30, 1986, is equal to 2-1/4% of the employee's average monthly compensation for the second ten years and 2-1/2% for all remaining years of service. For police and fire employees, the benefit for years of service through a total of ten years is equal to 2% of the employee's average monthly compensation and 2-1/2% for all remaining years of service.

Minimum benefits for employees eligible for retirement are $25 per month for each year of credited service.

Married members must receive their benefits in the form of a joint and survivor annuity unless their spouses consent to another form of benefit or another person is eligible for benefits under a qualified domestic relations order.

The Plan has two types of postretirement pension adjustments (PRPA). The automatic PRPA is issued annually to all eligible benefit recipients, when the cost of living increases in the previous calendar year. The automatic PRPA increase is paid beginning July 1 of each year. The discretionary PRPA may be granted to eligible recipients by the Plan Administrator, if the cost of living in the previous calendar year rises and the financial condition of the Plan permits. If both an automatic and discretionary PRPA are granted, and a retiree is eligible for both adjustments, the one that provides the retiree the greater increase will be paid.

(c) Postemployment Healthcare Benefits

Major medical benefits are provided to retirees without cost for all employees hired before July 1, 1986. Employees hired after July 1, 1986 with five years of credited service (or ten years of credited service for those first hired after July 1, 1996) must pay the full monthly premium if they

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are under age sixty, must pay half of the monthly premium if they are over age sixty but under age sixty-five, and receive benefits at no cost if they are over age sixty-five.

Prior to July 1, 1997, postemployment health-care benefits were provided by the payment of premiums to an insurance company. Beginning July 1, 1997, the Retiree Health Fund (RHF), an internal service fund of the State, was established. The RHF is self-funded and provides major medical coverage to retirees of the Plan. Retirees of three other State retirement plans also participate in the RHF. The Plan, along with the other participating plans, retains the risk of loss of allowable claims. Each year, RHF issues a publicly available financial report, which may be obtained by writing to the State of Alaska, Department of Administration, Division of Retirement and Benefits, P.O. Box 110203, Juneau, Alaska, 99811-0203 or by calling (907) 465-4460.

(d) Death Benefits

If an active Plan member dies from occupational causes, the spouse may receive a monthly pension equal to 40% of the Plan member's salary. When death is due to occupational causes and there is no surviving spouse, the Plan member's dependent child(ren) may receive the monthly pension until they are no longer dependents. The amount of the occupational death pension changes on the date the Plan member's normal retirement would have occurred if the Plan member had lived. The new benefit is based on the Plan member's average monthly compensation at the time of death and the credited service, including service that would have accrued if the Plan member had lived and continued to work until normal retirement. If the death was from nonoccupational causes, and the Plan member was vested, the spouse may receive a monthly survivor benefit based on a 50% joint and survivor option. If the Plan member is not married or vested, a lump sum death benefit is payable to the named beneficiary(ies).

(e) Disability Benefits

Active Plan members who become permanently disabled due to occupational or nonoccupational causes receive disability benefits until normal retirement age or when the service requirement for normal retirement is met. Although there are no minimum service requirements for Plan members to be eligible for occupational disability, Plan members must be vested to receive nonoccupational disability benefits. The monthly occupational disability benefit is equal to 40% of the Plan member's salary at the time of the disability. The nonoccupational disability benefit is based on the Plan member's service and salary at the time of disability. At normal retirement age, a disabled Plan member receives normal retirement benefits.

(f) Contributions

<u>Plan Member Contributions</u>

Contribution rates are 7.5% for peace officers and firefighters and 6.75% for other Plan members, as required by statute. The Plan member contributions are deducted before federal income tax is withheld. Contributions are col-

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lected by employers and remitted to the Plan and may be voluntarily or, under certain circumstances, involuntarily refunded to the employee or a garnishing agency sixty days after termination of employment. Plan member contributions earn interest at the rate of 4.5% per annum, compounded semiannually.

Employer Contributions

The Plan's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate assets to pay both pension and postemployment healthcare benefits when due. Employer contribution rates are level percentages of payroll and are determined using the projected unit credit actuarial funding method. The Plan uses the level dollar method to amortize the unfunded liability or the funding surplus over a rolling twenty-five year period.

(g) Administrative Costs

Administrative costs are financed through investment earnings.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Accounting

The Plan's financial statements are prepared using the accrual basis of accounting. Contributions are recognized in the period in which they are due. Benefits and refunds are recognized when due and payable.

(b) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions during the reporting period. Actual results could differ from those estimates.

(c) GASB Statements No. 25 and No. 26

Government Accounting Standards Board (GASB) Statements No. 25 and No. 26 require that plan net assets be split between pension and postemployment healthcare. To meet these requirements, plan assets, liabilities, revenues and expenses not specifically identifiable to either plan are allocated to the pension and postemployment healthcare plans based on their proportionate share of actuarial accrued liabilities.

(d) Investments

Security transactions and any resulting gains or losses are accounted for on a trade date (ownership) basis at the current fair value. Dividend income on domestic and international equity securities is accrued on the ex-dividend date. Interest in the international fixed income pool is accrued daily.

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Investments are recorded at fair value. Fair value is "the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller – that is, other than in a forced or liquidation sale."

As the emerging markets equity pool recognizes income, the per share value changes, resulting in the recognition of unrealized gains/ losses at the pool and participant level. When participants' shares in the pool are sold, previously unrealized income is realized at the participant level.

Income in the short-term fixed income pool is calculated daily and credited monthly to each participant. Total income, which includes interest and realized and unrealized gains and losses on securities, is calculated daily and distributed monthly to each participant on a pro rata basis.

Income in the retirement fixed income pool and the external domestic fixed income pool is calculated daily and is reinvested. Total income, which includes interest and realized and unrealized gains and losses on securities, is allocated daily to each participant on a pro rata basis but is not distributed.

Net appreciation (depreciation) is determined by calculating the change in the fair value of investments between the end of the year and the beginning of the year, less purchases of investments at cost, plus sales of investments at fair value.

Investment expense consists of those administrative expenses directly related to the Plan's investment operations.

Real estate investments include commingled real estate equities, separate account limited partnerships, mortgage loans and other real estate acquired by foreclosure and judgments. Commingled real estate equities and separate account limited partnerships are valued quarterly by public market quotations, where a quoted market exists, or by independent appraisers, and are periodically adjusted by trustees of the investments when market conditions change. The cost of commingled real estate equities and separate account limited partnerships securities is determined on the average cost basis. Mortgage loans are valued at their principal balance (cost) less an allowance for loan loss, the net result of which approximates fair value. The allowance for loan loss is considered by management to be sufficient to cover any losses to the mortgage loan portfolio. Real estate acquired by foreclosure and judgments is carried at estimated net realizable value.

Venture capital investments in the private equity pool are comprised of limited partnerships in privately held companies of which equity ownership is not traded on a national or international exchange. Investments in the private equity pool are valued quarterly by the general partners and investment sponsors. The private equity oversight manager is held to a standard of reasonable care in verifying that the general partners' valuations reasonably reflect the underlying value of the investments. The cost of investments in the private equity pool is determined on the average cost basis.

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The Plan holds shares, rather than specific securities, in the emerging markets equity pool, a closed-end mutual fund-like commingled equity investment pool. Underlying securities within the pool are priced on the last business day of each week and each month. Equity securities are valued using the last reported sale price on the exchange on which the securities are traded as of the close of business on the day the securities are being valued, or, in the absence of any sales price, at the last reported bid price. Fixed income securities are valued at prices obtained from a bond pricing service when such prices are available; otherwise, such securities are valued at the mid-point between the bid and asked price or at prices for securities of comparable maturity, quality and type. Short-term securities with 60 days or less to maturity are amortized to maturity based on cost. Securities expressed in terms of foreign currencies are translated into U.S. dollars at the prevailing market rates. Forward currency contracts are valued at the mid-point of representative quoted bid and asked prices. Securities and assets for which representative market quotations are not readily available are valued at fair value as determined in good faith under policies approved by the commingled equity fund's board of directors.

The fair value of all other debt and equity securities is determined by the custodial agent each business day. The custodian determines fair value using pricing services or prices quoted by one or more independent brokers. Equity securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates, if applicable, defaulting to current bid price if a particular security was not traded that day. Fair value of debt securities has been established as the midpoint between the bid and asked prices. The cost of debt and equity investments is determined on the average cost basis.

(e) Contributions Receivable

Contributions from Plan members and employers for service through June 30 are accrued. These contributions are considered fully collectible and, accordingly, no allowance for uncollectible receivables is reflected in the financial statements.

(f) Federal Income Tax Status

The Plan purports to be a qualified plan under Section 401(a) of the Internal Revenue Code and is exempt from federal income taxes under Section 501(a).

(g) GASB Statement No. 34

In June 1999, the GASB issued Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments* (GASB 34), its revolutionary new reporting model. The new model dramatically changes the presentation of governments' external financial statements. In the GASB's view the objective of the new model is to enhance the clarity and usefulness of governmental financial statements to the citizenry, oversight bodies, investors and creditors. As a component unit of the State of Alaska (State), the Plan is required to implement the standard concurrent with the State during the

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year ended June 30, 2002. The new reporting model fundamentally changes the format, content and basis of accounting used by state and local governments. For example, management's discussion and analysis (MD&A) will be a required part of the financial statements under GASB 34. The full impact of GASB 34 has not yet been determined.

(3) INVESTMENTS

GASB Statement No. 3 requires a disclosure regarding custodial credit risk to indicate the chance of loss in the event a financial institution or third party holding the Plan's deposits or securities fails. Deposits and those investments represented by specific, identifiable securities are classified into three categories of credit risk: Category 1 – Insured or registered, or securities held by the State or its custodian in the State's name; Category 2 – Uninsured or unregistered, with securities held by the counterparty's trust department (if a bank) or agent in the State's name; and Category 3 – Uninsured and unregistered, with securities held by the counterparty, or by its trust department (if a bank) or agent, but not in the State's name. Category 1 is the highest level of safekeeping security as defined by GASB.

At June 30, 2001 and 2000, the Plan's cash and cash equivalents and investments other than mortgage-related assets are represented by participation in investment pools rather than specific, identifiable securities. Although pooled investments represent the Plan's share of ownership in the pool rather than ownership of specific securities, all of the underlying securities in the pools in which the Plan participates are considered to be Category 1 as defined by GASB Statement No. 3, except: (A) investments in the mutual fund-like emerging markets equity pool which are considered to be Category 2, and (B) shares in the private equity pool and the real estate pool which, like the Plan's mortgage-related assets, are not transferable financial instruments and therefore cannot be categorized with regard to custodial credit risk.

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The cost and fair value of the Plan's investments at June 30, 2001 and 2000 are as follows:

	Cost	Fair Value
2001:		
Domestic equity pool	$ 2,961,249	3,335,990
Retirement fixed income pool	2,064,488	2,069,116
International equity pool	1,484,537	1,325,767
Real estate pool	539,404	588,545
International fixed income pool	417,952	384,827
Private equity pool	199,575	206,465
Emerging markets equity pool	89,983	72,557
External domestic fixed income pool	96,544	97,392
	$ 7,853,732	**8,080,659**
2000:		
Domestic equity pool	$ 2,844,774	3,754,045
Retirement fixed income pool	2,249,202	2,178,112
International equity pool	1,416,005	1,585,597
Real estate pool	443,062	467,789
International fixed income pool	445,608	402,545
Private equity pool	138,617	164,766
Emerging markets equity pool	89,601	97,644
External domestic fixed income pool	87,172	86,931
	$ 7,714,041	**8,737,429**

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(000's omitted)

During 2001 and 2000, the Plan's investments (including investments bought, sold, as well as held during the year) appreciated (depreciated) in value as follows:

	2001	2000
Investments measured by quoted fair values in an active market:		
Domestic equity pool	$(497,598)	312,667
Retirement fixed income pool	90,518	(63,976)
International equity pool	(321,990)	242,687
Real estate pool	11,458	3,829
International fixed income pool	(44,615)	(36,530)
Private equity pool	(2,248)	42,072
Emerging markets equity pool	(25,469)	14,323
External domestic fixed income pool	3,975	(682)
	$(785,969)	**514,390**

Based on the Plan's percentage of ownership in each investment pool as of June 30, 2001 and 2000, the Plan held no individual investments which exceeded 5% of net assets held in trust for pension and postemployment healthcare benefits.

The Alaska State Pension Investment Board (ASPIB) has statutory oversight of the Plan's investments and the authority to invest the Plan's monies. As the fiduciary, ASPIB has the statutory authority to invest the assets under the Prudent Investor Rule. Alaska Statute provides that investments shall be made with the judgment and care under circumstances then prevailing that an institutional investor of ordinary professional prudence, discretion and intelligence exercises in managing large investment portfolios. Actual investing is performed by the investment officers of the Division of Treasury of the Department of Revenue or by contracted external investment managers.

(4) POOLED INVESTMENTS

(a) Short-Term Fixed Income Pool

The Plan, along with other State funds, participates in an internally managed short-term fixed income pool, which was established March 15, 1993, with a start up unit price of $1 per share. Each participant owns shares in the pool, the number of which fluctuates daily with contributions, withdrawals and income. A share price of $1 is maintained, giving each participant one share for every dollar invested in the short-term fixed income pool. The assets of the short-term fixed income pool are comprised of money market instruments, U.S. Treasuries, U.S. Government agency debt, corporate debt and other U.S. dollar denominated bonds. At June 30, 2001 and 2000, the Plan has a .05% and .03% direct ownership in the short-term fixed income pool totaling $530 and $544, respectively. These amounts include interest receivable of $15 and $17, respectively.

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(000's omitted)

(b) Domestic Equity Pool

The Plan, along with three other State retirement systems, participates in an externally managed domestic equity pool. The pool was established July 1, 1991, with a start up unit price of $1,000 per share. Each manager may independently determine the allocation between equity and other permissible securities. All income, including interest, dividends and realized and unrealized gains and losses, is allocated daily to each participant on a pro rata ownership basis and is reinvested. At June 30, 2001 and 2000, the Plan's investment in the domestic equity pool totaled 66.16% and 65.67%, respectively, and consisted of the following:

	2001	2000
Domestic equity securities	$3,245,953	3,663,628
Convertible bonds	4,271	880
Available cash held in the short-term fixed income pool, other short-term debt instruments and currency	41,950	90,722
Net receivables (payables)	43,816	(1,185)
	$3,335,990	**3,754,045**

(c) Retirement Fixed Income Pool

The Plan, along with three other State retirement systems, participates in an externally managed retirement fixed income pool. The pool was established March 1, 1996, with a start up unit price of $1,000 per share. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of units of the pool outstanding on the valuation date. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the net asset value per share on the day of the transaction. At June 30, 2001 and 2000, the Plan's investment in the retirement fixed income pool totaled 66.53% and 66.25%, respectively, and consisted of the following:

	2001	2000
Mortgage related	$ 775,202	652,740
Corporate	656,149	518,425
U.S. Treasury	384,952	443,633
Yankees	69,813	266,902
Asset backed	68,267	24,771
U.S. government agency	67,114	211,779
Available cash held in the short-term fixed income pool	79,673	376,546
Net payables	(32,054)	(316,684)
	$2,069,116	**2,178,112**

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(000's omitted)

(d) International Equity Pool

The Plan, along with three other State retirement systems, participates in an externally managed international equity pool. The pool was established January 1, 1992, with a start up unit price of $1,000 per share. Each manager may independently determine the allocation between equities and other permissible securities. All income, including interest, dividends and realized and unrealized gains and losses, is allocated daily to each participant on a pro rata ownership basis and is reinvested. At June 30, 2001 and 2000, the Plan's investment in the international equity pool totaled 66.13% and 65.53%, respectively, and consisted of the following:

	2001	2000
International equity securities	$1,300,832	1,531,885
Available cash held in short-term debt instruments and foreign currency	22,860	50,084
Net receivables	2,075	3,628
	$1,325,767	**1,585,597**

(e) Real Estate Pool

The Plan, along with one other State retirement system, participates in an externally managed real estate pool. The pool was established June 27, 1997, with a start up unit price of $1 per share. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the net asset value per share on the day of the transaction. All income, including interest, income from operations, and realized and unrealized gains and losses, is allocated monthly to each participant on a pro rata ownership basis. All income is reinvested except for cash distributions which are transferred to the retirement fixed income pool based on a pro rata ownership in the originating pool. At June 30, 2001 and 2000, the Plan has 66.59% and 65.57% direct ownership in the real estate equity pool totaling $588,545 and $467,789, respectively.

(f) International Fixed Income Pool

The Plan, along with one other State retirement system, participates in an externally managed international fixed income pool. The pool was established March 3, 1997, with a start up unit price of $1,000 per share. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of units of the pool outstanding on the valuation date. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the net asset value per share on the day of the transaction. At June 30, 2001 and 2000, the Plan's investment in the international

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fixed income pool totaled 66.50% and 65.62%, respectively, and consisted of the following:

	2001	2000
International fixed income securities	$196,851	386,808
Available cash held in short-term debt instruments and foreign currency	4,004	2,945
Net receivables	183,972	12,792
	$384,827	**402,545**

(g) Private Equity Pool

The Plan, along with one other State retirement system, participates in an externally managed private equity pool. The pool was established April 24, 1998, with a start up unit price of $1,000 per share. Ownership in the pool is based on the number of shares held by each participant. Underlying assets in the pool are composed of venture capital, buyouts and special situation investments through limited partnership agreements. Contributions to and withdrawals from the pool are based on the net asset value per share on the day of the transaction. All income, including interest and realized and unrealized gains and losses, is allocated monthly to each participant on a pro rata ownership basis and is reinvested. At June 30, 2001 and 2000, the Plan has 66.44% and 65.50% direct ownership in the private equity pool totaling $206,465 and $164,766, respectively.

(h) Emerging Markets Equity Pool

The Plan, along with one other State retirement system, participates in an emerging markets equity pool. The pool was established May 2, 1994, with a start up unit price of $1,000 per share. The pool participates in two externally managed commingled investment funds through ownership of equity shares. The commingled funds, comprised of various institutional investors, invest in the equity markets of developing countries. At June 30, 2001 and 2000, the Plan has a 65% ownership in the pool totaling $72,557 and $97,644, respectively.

(i) External Domestic Fixed Income Pool

The Plan, along with three other State retirement systems, participates in an externally managed domestic fixed income pool. The pool was established June 25, 1999, with a start up unit price of $1,000 per share. The net asset value per share is determined by dividing the total fair value of the net assets of the pool by the number of units of the pool outstanding on the valuation date. Ownership in the pool is based on the number of shares held by each participant. Contributions to and withdrawals from the pool are based on the net asset value per share on the day of the transaction. At June 30, 2001 and 2000, the Plan's investment in the external

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domestic fixed income pool totaled 65.73% and 65.33%, respectively, and consisted of the following:

	2001	2000
Mortgage related	$ 49,391	44,088
Corporate	18,666	16,932
U.S. Treasury	17,333	11,600
U.S. government agency	3,930	4,253
Asset backed	3,619	6,820
Yankees	1,658	650
Municipal	557	975
Available cash held in short-term debt instruments	4,052	16
Net receivables (payables)	(1,814)	1,597
	$ 97,392	86,931

(5) FOREIGN EXCHANGE CONTRACTS AND OFF-BALANCE SHEET RISK

The Plan, through its investment in the international equity pool, entered into foreign currency forward contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing security positions in these currencies. The maturity periods for these contracts range from one to two months. The Plan had net unrealized gains with respect to such contracts, calculated using forward rates at June 30 as follows:

	2001	2000
Net contract sales	$ 5,258	12,340
Less: fair value	5,118	12,323
Net unrealized gains on contracts	$ 140	17

The counterparties to the foreign currency forward contracts consist of a diversified group of financial institutions. The Plan is exposed to credit risk to the extent of non-performance by these counterparties; however, the Plan considers the risk of default to be remote. The Plan's market risk is limited to the difference between contractual rates and forward rates at the balance sheet date.

(6) SECURITIES LENDING

Alaska Statute 37.10.071 authorizes the Board to lend assets, under an agreement and for a fee, against deposited collateral of equivalent market value. In January 2001 the Board entered into an agreement with State Street Bank and Trust Co. (the Bank) to lend marketable debt and equity securities. The Bank, acting as the Board's agent under the agreement, transfers securities to broker agents or other entities for collateral in the form of cash or securities and simultaneously agrees to return the collateral for the same securities in the future.

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At June 30, 2001, the fair value of securities on loan attributable to the Plan totals $674,797. The Board is able to sell any securities out on loan. There is no limit to the amount that can be loaned. U.S. dollar denominated securities loans are fully collateralized at not less than 102 percent of their fair value. Non-U.S. dollar denominated securities loans are fully collateralized at not less than 105 percent of their fair value. The Bank invests the cash collateral in a commingled investment pool; maturities of these investments generally did not match the maturities of the loaned securities because the lending agreements were terminable at will. The Bank may pledge or sell collateral upon borrower default. There is limited credit risk associated with the lending transactions since the Board is indemnified by the Bank against any loss resulting from counterparty failure or default on a loaned security subject to limitation relating to war, civil unrest or revolution, or beyond the reasonable control of the Bank. The Bank and the borrower receive a fee from earnings on invested collateral.

For the year ended June 30, 2001, there were no losses incurred as a result of securities lending transactions and there were no significant violations of legal or contractual provisions nor failures by any borrowers to return loaned securities.

(7) RETIREMENT INCENTIVE PROGRAM

House Bill 354 (Chapter 65, SLA 96) was passed on June 18, 1996, and provides for a retirement incentive program (RIP or program) for members of school district employers and employees of Mt. Edgecumbe and the Alaska Vocational Technical Center. The RIP encourages eligible employees to retire up to three years earlier than they had planned as a cost savings to the employer. The incentive program may be implemented if the program will produce an overall cost savings to the employer. The application and retirement deadlines are determined by the employer when they establish a program. The original application period for employees under House Bill 354 was June 30, 1996 through December 31, 1996. During fiscal year 1997, Senate Bill 130 (Chapter 92, SLA 97) was passed which amended the original program. Senate Bill 130 allowed for additional application periods on an "as needed basis" anytime through June 30, 1999.

Senate Bill 1003 (Chapter 4, FSSLA 96) was passed on June 28, 1996, and provides for a RIP for employees of the State, the University of Alaska and all employers other than school districts. Under this legislation, the State and University of Alaska could open a RIP application period on an "as needed basis" anytime between July 18, 1996 and June 30, 1999. The program was designed to allow State agencies to use the RIP in a strategic, targeted approach tailored to the specific budget and personnel situation of each agency. Some State agencies may determine that the RIP is not cost-effective for their agency and elect not to participate in the RIP. Other agencies may offer the RIP only in divisions or job classifications facing budget reductions or position cuts.

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Employers who participate in either of the RIP programs are required to reimburse the Plan for the actuarial equivalent of the difference between the benefits each employee receives after the addition of the retirement incentive under the program and the amount the employee would have received without the incentive, less any amount the employee was indebted as a result of retiring under the program. Reimbursements from employers are due in minimum equal annual installments so that the entire balance is paid within three years after the end of the fiscal year in which each employee retires. Employers are also required to reimburse the Plan for the estimated costs of administering the program. The Plan establishes a receivable for employer reimbursements and administrative costs as employees retire. During fiscal year 2000, the Plan recognized $13,880 of additions to plan net assets for contributions from employers for required reimbursements under the RIP. There were no additions to plan net assets during fiscal year 2001.

When employees terminate employment to participate in the program, they are indebted to the Plan for the following percentages of their annual compensation for the calendar year in which they terminate:

Police and fire members	22.50%
Other members	20.25%

Any outstanding indebtedness at the time an employee is appointed to retirement results in an actuarial adjustment of his/her benefit amount. During fiscal year 2000, the Plan recognized $810 of additions to plan net assets for contributions from employees related to the RIP. There were no additions to plan net assets during fiscal year 2001.

(8) COMMITMENTS AND CONTINGENCIES

(a) Commitments

The Plan, through its investment in the private equity pool, entered into agreements through an external investment manager to provide capital funding for limited and general partnerships as it continues to build a private equity portfolio. At June 30, 2001, the Plan's share of these unfunded commitments totaled $211,685 to be paid through the year 2006.

(b) Contingencies

The State is a defendant in a lawsuit filed by the Alaska Civil Liberties Union and six same-sex couples with regards to the statutes limiting retiree health insurance coverage to retirees and their spouses and dependents, thus excluding coverage for domestic partners of retirees. An adverse ruling against the State would increase the number of persons that would be covered by insurance paid by the Plan.

Although the ultimate outcome of the litigation discussed above is uncertain at this point in time, the Plan believes that an unfavorable outcome, if rendered, would not have a material adverse effect on its financial position or funding status. The Plan has not recorded an accrual related to the above lawsuit, because an unfavorable outcome in this matter is, in

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management's opinion, not considered probable but rather only possible, and the potential loss, if any, cannot be reasonably estimated at this time.

The Plan is a defendant in four similar lawsuits, three of which are class action suits. The lawsuits pertain to whether recent changes to the retiree health insurance program under the Plan resulted in violations of members' constitutional rights to retirement benefits. Subsequent to June 30, 2001, the Superior Court of the State of Alaska issued an order granting the plaintiffs' motion for partial summary judgment. The Plan has not recorded an accrual based on this unfavorable outcome as the potential loss cannot be reasonably estimated at this time and management intends to vigorously contest this decision.

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Required Supplementary Information

Schedule of Funding Progress
Pension Benefits
June 30, 2001 and 2000
(000's omitted)

Actuarial valuation year ended June 30	Actuarial value of plan assets	Actuarial accrued liabilities (AAL)	Funded excess (FE)/ (Unfunded actuarial accrued liabilities) (UAAL)	Funded ratio	Covered payroll	FE/(UAAL) as a percentage of covered payroll
1996	$3,804,973	3,594,706	210,267	105.8%	$1,221,866	17.2%
1997	4,287,497	4,031,527	255,970	106.3%	1,299,135	19.7%
1998	4,692,095	4,430,237	261,858	105.9%	1,235,439	21.2%
1999	4,992,453	4,730,841	261,612	105.5%	1,283,549	20.4%
2000	5,245,612	5,190,835	54,777	101.1%	1,321,480	4.1%

See accompanying notes to required supplementary information and independent auditors' report.

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Schedule of Funding Progress
Postemployment Healthcare Benefits
June 30, 2001 and 2000
(000's omitted)

Actuarial valuation year ended June 30	Actuarial value of plan assets	Actuarial accrued liabilities (AAL)	Funding excess (FE)/ (Unfunded actuarial accrued liabilities) (UAAL)	Funded ratio	Covered payroll	FE/(UAAL) as a percentage of covered payroll
1996	$1,466,280	1,385,252	81,028	105.8%	$1,221,866	6.6%
1997	1,597,991	1,502,589	95,402	106.3%	1,299,135	7.3%
1998	1,879,467	1,773,754	105,713	105.9%	1,235,439	8.6%
1999	2,023,887	1,917,832	106,055	105.5%	1,283,549	8.3%
2000	2,209,146	2,186,077	23,069	101.1%	1,321,480	1.7%

See accompanying notes to required supplementary information and independent auditors' report.

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Required Supplementary Information

Schedule of Employer Contributions
Pension and Postemployment Healthcare Benefits
June 30, 2001 and 2000
(000's omitted)

Year ended June 30	Pension annual required contribution	Postemployment healthcare annual required contribution	Total annual required contribution	Pension percentage contributed (note 3)	Postemployment healthcare percentage contributed (note 3)	Total percentage contributed (note 3)
1996	$107,058	40,582	147,640	100%	100%	100%
1997	104,409	40,454	144,863	100%	100%	100%
1998	69,259	25,958	95,217	100%	100%	100%
1999	69,337	27,860	97,197	100%	100%	100%
2000	63,344	25,740	89,084	105.2%	105.2%	105.2%
2001	65,151	26,477	91,628	105.3%	105.3%	105.3%

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(1) DESCRIPTION OF SCHEDULE OF FUNDING PROGRESS

Each time a new benefit is added which applies to service already rendered, an "unfunded actuarial accrued liability" is created. Laws governing the Plan require that these additional liabilities be financed systematically over a period of future years. Also, if actual financial experiences are less favorable than assumed financial experiences, the difference is added to the unfunded actuarial accrued liability.

In an inflationary economy, the value of the dollar is decreasing. This environment results in employee pay increasing in dollar amounts resulting in unfunded actuarial accrued liabilities increasing in dollar amounts, all at a time when the actual value of these items, in real terms, may be decreasing.

(2) ACTUARIAL ASSUMPTIONS AND METHODS

The actuarial valuation is prepared by William M. Mercer, Incorporated. The significant actuarial assumptions used in the valuations as of June 30, 2000 are as follows:

(a) Actuarial cost method – projected unit credit, unfunded actuarial accrued liability or funding excess amortized over a rolling twenty-five year period, which is an open amortization period.

(b) Mortality basis – 1994 Group Annuity Mortality Basic Table for males and females, 1994 base year. Deaths are assumed to be occupational 85% of the time for police and fire members and 35% for other members.

(c) Retirement age – retirement rates based on the 1997-1999 actual experience.

(d) Investment return – 8.25% per year, compounded annually, net of expenses.

(e) Health cost trend –

Fiscal Year	
00	8.5%
01	7.5%
02	6.5%
03	5.5%
04-08	5.0%
09-13	4.5%
14 and later	4.0%

(f) Salary scale – inflation 3.5%, productivity and merit (first five years) for police and fire members, 1% and 1.5%, respectively, and for all other members, productivity and merit (first five years) 0.5% and 1.5%, respectively.

(g) Total inflation – total inflation as measured by the Consumer Price Index (CPI) for urban and clerical workers for Anchorage is assumed to increase 3.5% annually.

(h) Cost of living allowance (domicile in Alaska) – 68% of those benefit recipients who are eligible for the allowance are assumed to remain in Alaska and receive the allowance.

(i) Contribution refunds – 100% of those employees terminating after age thirty-five will leave their contributions in the Plan and

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thereby retain their deferred vested benefit. All others who terminate are assumed to have their contributions refunded.

(j) Disability – assumptions are based upon the 1991-1995 actual experience of the Plan. Post-disability mortality in accordance with rates published by the Pension Benefit Guaranty Corporation to reflect mortality of those receiving disability benefits under Social Security.

(k) Asset valuation method – no asset gain or loss for the fiscal year is recognized if the expected actuarial value of assets plus (minus) the outstanding balance of previously amortized amounts is within a 5% corridor of the market value of assets. Any amount outside this 5% corridor is set aside and applied to the employer rate as a level percentage of pay over twenty years under the 1% population projection scenario. Valuation assets cannot be outside the range of 80% to 120% of the market value of assets.

(l) Valuation of medical benefits for retirees – a pre-age sixty-five cost and lower post-age sixty-five cost (due to Medicare) are assumed such that the total rate for all retirees equals the present premium rate assumption. These medical premiums are then increased with the health cost inflation assumption.

(m) 102% target funding ratio – the target unfunded (surplus) accrued liability is determined by first reducing the actuarial value of assets by 2.343757% and calculating the resulting unfunded (surplus) accrued liability. This unfunded (surplus) liability is then loaded by 6% to account for the 2-year delay in employer contributions. Both of these factors are determined empirically from the actuarial projection valuation. This target unfunded accrued liability (surplus) is then added to the actuarial value of assets to determine the target accrued liability. This target accrued liability is the basis for the determination of the employer contribution rate before the rate is adjusted for the deferred gains or losses outside the 5% corridor as discussed above.

(n) Spouse's age – wives are assumed to be four years younger than husbands.

(o) Dependent children – benefits to dependent children have been valued assuming members who are not single have one dependent child.

(p) Post-retirement pension adjustment – 50% and 75% of assumed inflation is valued for the automatic Post-Retirement Pension Adjustment (PRPA).

(q) Expenses – expenses are covered in the investment return assumption.

(r) Marital status – 75% of participants are assumed to be married.

(s) Total turnover – assumptions are based upon the 1997-1999 actual withdrawal experience.

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(t) New entrants – growth projections are made for the active PERS population under three scenarios:

Pessimistic:	0% per year
Median:	1% per year
Optimistic:	2% per year

(u) Participant data – for the June 30, 2000 actuarial valuation, data as of June 30, 1999 was projected one year using standard actuarial techniques. The active population count was assumed to increase by 1.72% (quadratic extrapolation over the most recent valuation dates). Actual CPI data was used to estimate new PRPA benefits for participants retired as of June 30, 1999.

The assumptions and methods, when applied in combination, fairly represent past and anticipated future experience of the Plan. The foregoing actuarial assumptions are based on the presumption that the Plan will continue. Were the Plan to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated benefits.

All significant accounting policies, benefit provisions and actuarial assumptions are the same for the required supplementary information and the financial statements except as follows:

Effective June 30, 1994, there was a change in the asset valuation method. The revised asset valuation method smoothes the difference between expected investment return and actual return during a given year by spreading the results over five years by recognizing 20% of the investment gain or loss in each of the current and preceding four years.

Effective June 30, 1996, the investment return was increased from 8% to 8.25% per year. Disability assumptions were revised based on actual experience in 1991-1995. In addition, the amortization period for funding surpluses was changed from five years to a rolling twenty-five year period.

Effective June 30, 1998, the following changes were made:

- The asset valuation method was changed. The new asset valuation method produces no gains or losses for a fiscal year if the expected actuarial value of assets plus (minus) any deferred gains (losses) is within a 5% corridor of the market value. Expected assets outside this corridor are amortized over 20 years as a level percent of pay and applied directly to the consolidated employer rate. The gain (loss) amount that is set aside is not expected to be offset by any future gains (losses). The method is restarted if this is not the case. The old asset valuation method recognized 20% of the investment gain or loss in each of the current and preceding four years. All assets were valued at fair value. Valuation assets could not be outside a range of 80% to 120% of the fair value of assets.

- The target-funding ratio was changed from 100% to 102%.

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Effective June 30, 2000, the following changes were made:

- The mortality basis was changed from the 1984 Unisex Pension Mortality Table to the 1994 Group Annuity Mortality Basic Table, 1994 base year.
- The turnover assumptions were revised based on actual withdrawal experience in 1997-1999.
- The retirement age assumptions were revised based on actual experience in 1997-1999.
- The health cost trend assumptions were changed for fiscal years 2009 and later from an ultimate rate of 4.5% to 4.5% for fiscal years 2009-2013 and 4% for all subsequent fiscal years.
- The salary scale assumptions were changed. The inflation assumption was changed to 3.5% from 4%, the productivity and merit (first five years) assumptions of 0.5% and 1%, respectively, were broken out for police/fire members and other members. Productivity and merit (first five years) for police/fire members and other members were set at 1% and 1.5%, and 0.5% and 1.5%, respectively.
- The total inflation assumption was changed from 4% to 3.5%.
- The cost of living allowance was decreased from 71% to 68%.
- Disabilities are no longer assumed to be occupational 85% of the time for police and fire members and 35% for other members.
- The percentage used to reduce the actuarial value of assets in the target unfunded (surplus) accrued liability calculation was increased to 2.343757% from 2.296%.
- For the June 30, 2000 actuarial valuation, data as of June 30, 1999 was projected one year using standard actuarial techniques. The active population count was assumed to increase by 1.72% (quadratic extrapolation over the most recent 3 valuation dates). Actual CPI data was used to estimate new PRPA benefits for participants retired as of June 30, 1999.

(3) ENHANCED ACTUARIAL PROJECTION SYSTEM

The Plan's actuary, at the request of the Public Employees Retirement Board, uses an enhanced actuarial projection system to determine annual employer contribution rates. Although the same actuarial cost method is used by the Plan's actuary, the enhanced system projects population growth patterns and their associated liabilities twenty-five years into the future.

The purpose of the enhanced actuarial projection system is to level out contribution rates in order to provide employers with a more stable long-term contribution pattern.

The Plan's utilization of the enhanced actuarial projection system resulted in 1996-1999 employer contributions being equal to the annual required contribution and 2000 and 2001 employer contributions being more than the annual required contribution.

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Schedule of Administrative and Investment Expenses

Year ended June 30, 2001
with comparative totals for 2000
(000's omitted)

	Administrative expenses	Investment expenses	Totals 2001	Totals 2000
Personal services:				
Wages	$ 2,029	726	2,755	2,571
Benefits	743	217	960	895
Other	8	-	8	6
Total personal services	2,780	943	3,723	3,472
Travel:				
Transportation	48	41	89	116
Per diem	35	40	75	89
Moving	-	5	5	4
Honorarium	11	11	22	9
Total travel	94	97	191	218
Contractual services:				
Management and consulting	218	17,568	17,786	17,738
Accounting and auditing	35	698	733	759
Other professional services	494	52	546	231
Data processing	358	19	377	204
Communications	198	63	261	275
Advertising and printing	18	173	191	352
Rentals/leases	105	61	166	73
Legal	53	12	65	92
Medical specialists	52	-	52	76
Repairs and maintenance	12	-	12	18
Transportation	3	3	6	9
Other services	15	116	131	112
Total contractual services	1,561	18,765	20,326	19,939
Other:				
Equipment	155	42	197	126
Supplies	82	16	98	73
Total other	237	58	295	199
Total administrative and investment expenses	**$ 4,672**	**19,863**	**24,535**	**23,828**

See accompanying independent auditors' report.

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Schedule of Payments to Consultants Other than Investment Advisors

Years ended June 30, 2001 and 2000 (000's omitted)

Firm	Services	2001	2000
State Street Bank and Trust Company	Custodian banking services	$ 841	1,131
William M. Mercer, Inc.	Actuarial services	218	271
The Retirement Concepts Group, Ltd.	Data processing consultants	202	118
Powertech Toolworks, Inc.	Data processing consultants	7	90
Wohlforth, Vasser, Johnson and Brecht	PERS Board legal services	55	50
KPMG LLP	Auditing services	51	49
State of Alaska, Department of Law	Legal services	57	25
		$ 1,431	1,734

See accompanying independent auditors' report.